

5 August 2004

Mr Jonathan G. Katz
Securities and Exchange Commission
450 Fifth Street
NW
Washington
DC 20549-0609

By email: rule-comments@sec.gov

Dear Mr Katz

File No. PCAOB-2004-005: PCAOB Rulemaking Docket No. 012

PCAOB Auditing Standard No. 3: Audit Documentation and an Amendment to AU sec. 543 of the Interim Auditing Standards

The Institute of Chartered Accountants in England & Wales (ICAEW) is pleased to comment on the SEC's exposure of the PCAOB's Auditing Standard No. 3. The ICAEW is the largest individual body of professionally qualified accountants in Europe with over 126,000 members who work in many sectors in business and the public sector, as well as practising as accountants and auditors. We operate under a Royal Charter that requires us to act in the public interest.

Improvements to the audit documentation standard made by the PCAOB

We commented to the PCAOB on 20 January 2004 on its exposure of the audit documentation standard. We are pleased that many improvements have been made in the standard approved by the PCAOB. In particular, requirements relating to the scope of documentation and the retention and review of documentation by group auditors have been amended. We also welcome the removal of the 'rebuttable presumption' that failure to document work performed indicates that the work was not performed. We are greatly encouraged that concerns which we and others expressed in these areas have been taken into account in the final standard.

Outstanding issues

The approval of this standard by the SEC will mark an important step in restoring investor confidence in audit quality. Nevertheless, we believe that there is a real risk that some of the standard's requirements may result in a shift of focus away from audit quality towards compliance with the standard for its own sake. This is because of the way that the overriding requirements of the standard are expressed and because of the interaction of the documentation standard with PCAOB Rule 3101.



1. Overriding requirements of the standard

We believe that the overriding purpose of audit documentation is to support the basis for the auditor's conclusions. The first comment in our letter to the PCAOB of 20 January 2004 dealt with this issue. The standard approved by the PCAOB states that audit documentation should 'demonstrate that the engagement complied with the standards of the PCAOB'. We agree with this requirement, but we do not agree that it should detract from, or have equal status with, the overriding purpose, which is for audit documentation to support the basis for the auditor's conclusions. Paragraph 5 of the standard lists the compliance requirement first and support of audit conclusions second. We remain concerned that this presentation will foster an inappropriate view of the objective of an audit. The primary objective is the provision of a high quality audit opinion to investors, not compliance with standards. There is a danger that a focus on compliance with standards will result in 'defensive auditing' and the performance of unnecessary audit procedures and the production of unnecessary audit documentation solely for the purposes of compliance.

2. Proposed PCAOB Rule 3101 '*Certain Terms Used in Auditing and Related Professional Practice Standards*'

PCAOB Rule 3101, on which we are submitting a separate response, states that failure to discharge a presumptively mandatory responsibility is a violation of the relevant standard and Rule 3100 unless the auditor demonstrates that, in the circumstances, compliance with the specified responsibility was not necessary to achieve the objectives of the standard. The rule does not specify *how* auditors should demonstrate this but by inference, demonstration must be in writing and must be more than a simple 'not applicable' statement. The effect of this could be to prompt auditors, particularly auditors of smaller entities, to produce extensive and unnecessary documentation in circumstances where a procedure is not followed simply because it is not applicable.

Promoting high quality audits

We encourage the SEC staff and Commissioners to emphasise in their public pronouncements the statements in paragraph 2 of the standard that audit documentation is the written record of the basis for the auditor's conclusions and is the basis for the review of the quality of the work.

Moreover, we encourage the SEC and the PCAOB to consider making a commitment to a timely review of the application of the standard to assess whether it has resulted in form and quantity of documentation prevailing over substance and quality.

These measures would together provide an appropriate signal to the auditing profession firms, and to the investors whom they serve, that auditing is not to be reduced to a low value activity which is unattractive to the brightest and best because it is driven by documentation of compliance with standards rather than the exercise of independent judgement.

We hope you find these comments helpful and we welcome continued dialogue with the SEC and the PCAOB on how, in the interests of investors globally, we can promote auditing of the highest quality.

Yours sincerely

A handwritten signature in cursive script that reads "Robert Hodgkinson".

Robert Hodgkinson
Director, Technical
Direct line: + 44 20 7920 8492
e-mail: robert.hodgkinson@icaew.co.uk

cc:

SEC Chairman William H. Donaldson

SEC Commissioners Paul S. Atkins, Cynthia A. Glassman, Roel C. Campos, Harvey J. Goldschmid

PCAOB Chairman William J. McDonough